



STATE OF MICHIGAN

DEPARTMENT OF HEALTH AND HUMAN SERVICES
LANSING

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IV-D MEMORANDUM 2016-020

TO: All Friend of the Court (FOC) Staff
All Office of Child Support (OCS) Staff
All Michigan State Disbursement Unit (MiSDU) Staff

FROM: Erin P. Frisch, Director
Office of Child Support

DATE: June 24, 2016

SUBJECT: Limit on Holding Potentially Fraudulent Federal Tax Refund
Offset (FTRO) Receipts, and Revisions to the FTRO Fraud
Process

UPDATE(S):

☐ Manual

☐ Form(s)

RESPONSE DUE: None

POLICY EFFECTIVE DATE: Upon receipt

PURPOSE:

This IV-D Memorandum announces revised policy on the federal tax refund offset (FTRO) fraud process. The federal Office of Child Support Enforcement (OCSE) recently published [Action Transmittal \(AT\)-16-03, *Timeframe to Distribute Tax Offsets Referred for Fraud*](#). This AT limits the amount of time a state can hold potentially fraudulent FTRO receipts¹ that are referred to the Internal Revenue Service (IRS). A state can hold these receipts up to six months from the date the state receives the FTRO. Prior to this AT, a state could hold potentially fraudulent FTRO receipts for an indefinite period of time.²

This policy change directly impacts OCS Central Operations' procedures. However, all IV-D workers should be aware that some FTRO receipts that are on hold for potential or confirmed fraud will be released and distributed after six months, regardless of the fraud status.

¹ OCSE AT-16-03 refers to potentially fraudulent receipts as "suspicious tax refund offsets."

² Ref: [Dear Colleague Letter \(DCL\)-11-17, *Erroneous Federal Tax Refund Offsets Based Upon Fraudulent Returns*](#).

This IV-D Memorandum describes the IRS interim final rule³ that imposes a time limit on the IRS's ability to reverse fraudulent FTRO receipts. The IRS must reverse these receipts within six months of the date the IRS notifies the Bureau of the Fiscal Service (BFS)⁴ that the offset is erroneous. This memorandum also explains the changes to Michigan's FTRO fraud process that have resulted from the IRS interim final rule.⁵

In addition, this IV-D Memorandum discusses:

- OCS Central Operations' process for monitoring and manually releasing FTRO receipts that are on hold for greater than six months;
- OCS Central Operations' process for handling confirmed fraudulent receipts received prior to January 1, 2016;⁶
- Differences between the Michigan Child Support Enforcement System's (MiCSES') distribution of FTRO receipts (TANF⁷ and non-TANF) and BFS's⁸ distribution of FTRO receipts;
- BFS's procedures for offset reversals and OCS Central Operations' process for responding to BFS inquiries; and
- Enhancements to the State Services Portal (SSP)⁹ and the IRS Collection and Adjustment file.¹⁰

OCS will update Section 6.21 of the *Michigan IV-D Child Support Manual* in the near future to incorporate the information in this memorandum.

DISCUSSION:

In December 2013, OCS implemented a process to automatically identify potentially fraudulent FTRO receipts and place them on hold until OCSE confirmed that the receipts were fraudulent or valid. It is important to identify and hold potentially fraudulent FTRO receipts because the IRS reverses FTRO receipts it confirms are fraudulent. If the IRS reverses an FTRO receipt that has been disbursed to the custodial party (CP)

³ Ref: [OCSE DCL-15-21, Offset of Tax Refund Payments to Collect Past-Due Support Interim Final Rule](#); and Federal Register (FR) 81436-81465.

⁴ BFS is a bureau of the Department of Treasury. BFS, OCSE, and the IRS administer the FTRO program. The Financial Management Service (FMS) previously performed the FTRO services that BFS performs today.

⁵ OCS announced this rule in [IV-D Memorandum 2016-006, Updates to the Federal Tax Refund Offset \(FTRO\) Fraud Process and to Section 6.21, "Tax Refund Offset," of the Michigan IV-D Child Support Manual](#) but instructed IV-D workers to take no action based on the rule. Since that time, OCSE has published guidance regarding the rule; therefore, the IV-D program must take action.

⁶ January 1, 2016 is the date that the IRS interim final rule became effective.

⁷ TANF is Temporary Assistance for Needy Families.

⁸ BFS forwards the FTRO receipts to the state on behalf of OCSE. BFS also processes reversal requests from the IRS.

⁹ Ref: [Section 3.06, "State Services Portal \(SSP\)," of the Michigan IV-D Child Support Manual](#) for more information about the SSP.

¹⁰ This file contains the FTRO receipts that will be processed in MiCSES. Ref: [Section 6.21, "Tax Refund Offset," of the Michigan IV-D Child Support Manual](#) for more information on this file.

rather than placed on hold, the Michigan IV-D program incurs financial losses.¹¹ Recently, OCSE published AT-16-03 to limit the duration of the hold period to six months from the date the state received the offset. OCSE also states in the AT that if the IRS has not completed its fraud investigation or reversed the offset after six months, the state must distribute the payment. OCSE based its guidance on the IRS interim final rule that amended a Treasury rule (31 Code of Federal Regulations [CFR] 285.3) and became effective January 1, 2016.

The amended Treasury rule imposed a six-month limit on the IRS to recoup erroneous FTROs from a state if the state has forwarded the funds to CPs. The rule impacts how the IRS will handle offset reversals. BFS, OCSE, and the states have worked together to create and implement an offset reversal process that is consistent with the rule. The rule does not apply to FTROs from joint tax returns because the IRS may reverse an FTRO for an injured spouse claim¹² greater than six months from the date of the offset.

A. Processing FTROs Subject to the Six-Month Hold Restriction

Prior to March 2016, OCS Central Operations manually placed *Unidentified Federal Tax Offset* (UFTO) holds on all potentially and confirmed fraudulent FTRO receipts. In March 2016, MiCSES began automatically placing an *FTRO Tax Fraud Process* (STFP) suspense hold on FTRO receipts it identified as potentially or confirmed fraudulent. OCS Central Operations will continue to monitor both types of holds.

1. UFTO Holds Between January 1, 2016 and March 2016

OCS Central Operations will manually monitor the FTRO receipts with a UFTO hold to ensure that the receipt is not held for a period greater than six months from the date of receipt. If the IRS confirms a receipt is fraudulent within the six-month period, OCS Central Operations will wait for the offset reversal.¹³ If an offset reversal is received within the six-month timeframe, OCS Central Operations will manually process the offset reversal per current procedures. If the IRS has not completed its fraud investigation or sent an offset reversal within six months from the date MiCSES initially processed the receipt, then OCS Central Operations will release the UFTO hold and MiCSES will distribute¹⁴ the payment regardless of the receipt's fraud status.

2. STFP Holds After March 2016

The STFP hold will remain on the FTRO receipt until one of the following occurs:

¹¹ Ref: Subsection 10 of Section 6.21 of the *Michigan IV-D Child Support Manual* for more information about holding potentially fraudulent FTROs.

¹² Ref: Subsection 9.3 of Section 6.21 of the *Michigan IV-D Child Support Manual* for more information about joint tax returns.

¹³ Offset reversals are also referred to as negative tax refund offsets.

¹⁴ MiCSES will distribute and disburse the receipt according to current distribution rules. Ref: [MiCSES Allocation/Distribution Hierarchies table](#) for more information about distribution rules.

- The receipt is confirmed fraudulent by the IRS and MiCSES processes an offset reversal;
- OCS Central Operations manually removes the hold after the IRS confirms the receipt is valid; or
- OCS Central Operations manually releases the hold after six months from the date of receipt because the IRS has not completed its fraud investigation and/or sent an offset reversal.

OCS Central Operations staff will manually monitor the FTRO receipts on STFP hold to ensure the receipt is not held for a period greater than six months. MiCSES updates are required to automatically limit the STFP hold to six months.¹⁵ Until these updates are implemented, OCS Central Operations will continue to manually monitor the STFP hold and release it after six months whether or not the fraud status is “Confirmed Fraud” or “Potential Fraud.”

B. Confirmed Fraudulent FTRO Receipts Received Prior to January 1, 2016

As of January 1, 2016, the effective date of the IRS’s interim final rule, Michigan and many other states held for over six months the FTRO receipts that the IRS confirmed fraudulent but for which the IRS did not process an offset reversal.¹⁶ OCSE provided the states the option of either distributing the FTRO funds or forcing a reversal of the receipts (i.e., requesting that the IRS process an offset reversal).

OCS opted to force a reversal of the receipts received prior to January 1, 2016 that were greater than six months old. Reversing rather than distributing these receipts would limit OCS’s possible financial liability if the IRS decided to reverse the FTROs after OCS had forwarded the receipts to CPs. Per OCSE’s request, OCS Central Operations sent a list of the Treasury Offset Program (TOP) Trace numbers associated with these receipts to OCSE on April 26, 2016. OCSE forwarded the list to BFS.

BFS will process a reversal request for each of the receipts, and OCS Central Operations will manually process the reversals in MiCSES per existing procedures.

C. TANF and Non-TANF FTRO Distribution

1. Bureau of the Fiscal Service (BFS)

When BFS determines that an FTRO receipt will be applied to a past-due child support debt, it will review the TANF and non-TANF arrears Michigan submitted for that non-custodial parent (NCP). The debt with the earliest submission date,

¹⁵ OCS has entered Help Desk ticket INC491760 to automatically limit the duration of the STFP hold and automate the steps to process the receipts when the hold expires.

¹⁶ The interim final rule did not apply to these receipts because Michigan received them prior to the effective date of the rule.

whether TANF or non-TANF, will be first in the distribution of offsets. BFS will distribute FTRO receipts to the state IV-D program on arrears with earlier submission dates before those with later submission dates. For example, if an NCP has both TANF and non-TANF arrears, and the state submits the non-TANF arrears for FTRO to BFS first,¹⁷ BFS will distribute FTRO receipts based on the non-TANF arrears. However, MiCSES distributes the FTRO receipts as described below.

2. MiCSES

When MiCSES receives the FTRO receipts, it distributes them according to its distribution rules.¹⁸ Therefore, even if BFS distributes the FTRO receipt for the non-TANF arrears first, MiCSES may distribute the funds to the TANF arrears first. This difference may impact OCS Central Operations' response when BFS sends an inquiry about whether Michigan has disbursed FTRO funds.

D. Bureau of the Fiscal Service (BFS) Procedures

In February 2016, OCSE notified states of BFS's new procedures for IRS reversal requests that are greater than six months from the offset date.¹⁹ Only OCS Central Operations staff are responsible for implementing the BFS procedures and responding to the inquiries. However, other IV-D workers may notice that the IRS is reversing FTRO receipts that are six months or older as a result of the procedures. The BFS procedures do not apply to:

- Reversals from joint tax returns;
- Reversals that BFS receives and processes prior to six months from the offset date;
- Partial offsets returned to BFS for bad addresses or incorrect bank account information;²⁰ and
- Administrative offset reversals.²¹

1. Response to BFS Inquiries on TANF FTROs

BFS will email the designated IV-D worker in OCS Central Operations to inquire whether Michigan disbursed the FTRO receipt to the CP when:

- BFS determines that a confirmed fraudulent FTRO receipt was applied to TANF arrears that Michigan submitted (Ref: Section C above); and
- The current date is greater than six months from the offset date.

¹⁷ Michigan submits TANF arrears and non-TANF arrears separately for FTRO.

¹⁸ Ref: MiCSES Allocation/Distribution Hierarchies table for more information about distribution rules.

¹⁹ BFS will process IRS reversal requests on receipts that are less than six months from the offset date without regard to whether the state has distributed the funds.

²⁰ These types of offsets are usually resolved within 30 days.

²¹ Michigan does not participate in the Administrative Offset program.

OCS Central Operations will research the receipt to determine if MiCSES disbursed all, part or none of the receipt to a CP and will appropriately respond to BFS within two to three business days of receiving the email request.

- a. If OCS Central Operations confirms that all of the FTRO receipt has been disbursed to a CP, then BFS will reject the IRS's request for a reversal.
- b. If OCS Central Operations confirms that part of the FTRO receipt has been disbursed to a CP, then BFS will process the undisbursed portion of the FTRO and will reject the IRS's request for reversal of the disbursed portion.
- c. If OCS Central Operations confirms that all of the FTRO receipt has been disbursed to the state, then BFS will process the IRS's request for a reversal.

2. Non-TANF FTROs

BFS will reject all reversal requests from the IRS and will not contact OCS Central Operations on FTROs when:

- BFS determines the FTRO was applied to non-TANF arrears that Michigan submitted (Ref: Subsection C above); and
- The current date is greater than six months from the offset date.

E. Updates to the IRS Collection and Adjustment File and the State Services Portal (SSP)

OCSE added the BFS reversal reason codes to the IRS Collection and Adjustment file.²² The reversal reason codes are also available in the Federal Collections and Enforcement Application on the SSP.²³ The reversal codes are federal tax information (FTI)²⁴ and will be available only to users with Full FTRO access to the Federal Collections and Enforcement application. The IV-D worker can use the reversal reason codes to learn why an offset reversal occurred. There are now five reversal reason codes:

- 0001 – IRS Injured Spouse;
- 0002 – IRS Other Reason (less than six months);
- 0003 – State Approved IRS Partial Reversal (after six months);

²² Help Desk Ticket 491007 has been entered to enhance MiCSES to accept and display the reversal reason codes in the IRS Collection and Adjustment file.

²³ Ref: Section 3.06 of the *Michigan IV-D Child Support Manual* for more information about the Federal Collections and Enforcement application.

²⁴ Ref: [Section 1.10, "Confidentiality/Security," of the Michigan IV-D Child Support Manual](#) for more information on FTI and confidentiality.

- 0004 – State Approved IRS Full Reversal (after six months);²⁵ and
- 0005 – BFS Initiated Reversal²⁶ (incorrect bank account or address).

Reversal reason codes 0002, 0003 and 0004 refer to full or partial reversals of confirmed fraudulent FTROs. OCS Central Operations will monitor the reversal reason codes through the SSP to ensure that the new processes are working as designed.

NECESSARY ACTION:

Retain this IV-D Memorandum until further notice.

REVIEW PARTICIPANTS:

Enforcement Work Improvement Team (WIT)
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SUPPORTING REFERENCES:

Federal
42 USC 664(a)(3)(B)
31 CFR 285.3
45 CFR 303.72 (h)(5)
FR 81436-81465

OCSE AT-16-03

OCSE DCL-11-17
OCSE DCL-15-21

²⁵ Codes 0003 and 0004 are used when OCS Central Operations has confirmed that all or a portion of the FTRO funds has not been disbursed.

²⁶ The interim final rule does not apply to these reversals; they can be reversed after six months from the date of receipt whether or not they have been disbursed to a CP.

State
None

ATTACHMENT(S):

None

EPF/VPW